VZCZCXRO1829
PP RUEHPA
DE RUEHUJA #1735/01 2421502
ZNY CCCCC ZZH
P 291502Z AUG 08
FM AMEMBASSY ABUJA
TO RUEHC/SECSTATE WASHDC PRIORITY 3831
INFO RUEHZK/ECOWAS COLLECTIVE PRIORITY
RUEHOS/AMCONSUL LAGOS PRIORITY 9875
RUCPDOC/DEPT OF COMMERCE WASHDC PRIORITY
RUEATRS/DEPT OF TREASURY WASHDC PRIORITY

C O N F I D E N T I A L SECTION 01 OF 02 ABUJA 001735

NOFORN
SIPDIS

DEPT PASS TO USTR-AGAMA
TREASURY FOR PETERS AND HALL
DOC FOR 3317/ITA/OA/KBURRESS AND
3130/USFC/OIO/ANESA/DHARRIS

E.O. 12958: DECL: 08/30/2118
TAGS: EFIN ECON EINV PGOV NI
SUBJECT: NIGERIA: CENTRAL BANK CANCELLATION OF UNIFORM
ACCOUNTING YEAR RAISES DOUBTS ABOUT THE HEALTH OF BANKS

REF: A. ABUJA 1695
¶B. ABUJA 1599
¶C. ABUJA 372
¶D. LAGOS 290
¶E. LAGOS 266
¶F. 07 ABUJA 1865

Classified By: Economic Counselor Bob Tansey, reasons 1.4 (b) and (d)

¶1. (C/NF) Summary. The Central Bank of Nigeria (CBN) recently canceled the uniform accounting year requirement for banks and discount houses. Banks and discount houses were expected to adopt December 31, 2008 as the common accounting year end. CBN announced that current interest rate trends arising from desperation of banks to shore up their deposit base necessitated the new decision. Embassy and ConGen Lagos contacts say that rising interest rates due to interbank lending were not the primary reason for the CBN's reversal. Banking industry contacts said CBN, banks, and other players were concerned that enforcing the accounting year requirement would lead to further bank consolidation, and specifically to bank failures. One contact said that "Godfathers" benefiting from zero interest rate loans did not want further CBN scrutiny of banks, and therefore arranged the cancellation of the common accounting year. End Summary.

¶2. (SBU) On August 5, CBN announced the cancellation of the requirement of a uniform accounting year for all banks and discount houses in Nigeria. CBN stated it predicated the decision on the observed unhealthy trend in the industry whereby some banks were mobilizing deposits at very high interest rates that were inconsistent with economic fundamentals, which was becoming a threat to market stability. CBN stated that in order to overcome this treat to market stability, each bank and discount house is now at liberty to adopt it's own accounting year end as it deems appropriate and inform the CBN accordingly. On July 23, CBN had earlier announced a postponement of the commencement of the policy from December 2008 to December 2009.

The Genesis of the Policy

¶3. (U) The requirement for a common year end was agreed by the CBN and CEOs of banks and discount houses at the Banker's Committee meeting of January 2008. Analysts and the public at large welcomed the requirement as a way of determining which bank was the actual industry leader because a common reporting period would provide a common yardstick to assess the strength of each of the banks.

¶4. (U) Nigerian banks post-consolidation have been claiming industry leadership on various criteria such as deposit base, shareholders' funds, asset quality, return on equity, and a host of other indices. It was difficult to ascertain the genuine industry leader in any category because the banks had different accounting year ends, and industry observers had was alleged that some banks were able to exaggerate their profile on the strength of borrowing from the inter-bank market to make their books look good as their financial year end approached.

¶5. (SBU) The positive response to the measure by industry analysts and the public was actually short lived when it was observed that in a bid to justify their books (assumed to have been cooked historically), some banks were mobilizing deposits at higher than market interest rates well beyond economic fundamentals. Banks took such actions because inter-bank borrowing would not be available to them once the common year end commenced. The common accounting year deadline also fueled intense competition in the industry for banks to mobilize deposits. Some banks were offering as much as 17 percent on time deposits and interest rates on loans were inching close to 30 percent until the CBN announced the policy had been canceled. The common year end policy had unleashed frenzy for deposit mobilization by banks at very high interest rate. Interest charged on loans had to be increased in a bid to avoid asset-liability mismatch. This was way out of line with fundamentals and was hurting the real sector that was already grappling with infrastructure challenges. The CBN said it had to wade in to ensure price stability in the light of inflationary pressures.

More than Meets the Eye

¶6. (C/NF) Industry analysts and a commercial bank official told Lagos Econoffs August 30 that rising interest rates were not the primary reason for the CBN policy reversal. The CBN could have taken other measures to make funds available to the banks without fueling inflation. Banks had been making uneconomic moves in the spirit of "bigger is better" which could have come to light under the common accounting year. The greatest fear was a bank failure leading to a domino effect. One analyst said that CBN Governor Soludo ultimately shied from the stronger accounting oversight out of concern that further consolidation (read failures) would add to the already strong criticism of Soludo for other measures, including the failure of northern banks in the earlier consolidation. An industry analyst speaking to Abuja Econ Deputy recently suggested the possibility of other sweetheart deals being covered up by the cancellation decision. He alleged that "Godfathers" benefiting from zero interest rate loans had sent intermediaries to speak to Finance Minister Usman and Chief Economic Advisor Yakubu about the impending common accounting year, and those intercessions had led to the cancellation. At least one senior CBN official told Embassy on August 29 that he disagreed with the cancellation decision, though he based his concern on the original goal of judging the health of the banks by a common standard.

Comment

¶7. (C/NF) The actions by banks in response to the uniform accounting year has led to questions being asked on the health of the banks. Some Nigerians opine and correctly so, that the CBN might be over-estimating the success of consolidation, is be lax in supervising the banks. JPMorgan sponsored a major report which came out in May and questioned the overall health of the sector and some individual banks. "The Economist" just had an article on the same theme. Renaissance Capital published a rosier report on Nigeria's banks about the same time as the JPMorgan report; local

bankers say the truth lies inbetween those two pieces. For uniform accounting, though much needed, to jolt the industry this much shows that some banks within the system still render false financial reports and are not as healthy as the public had been made to believe post-consolidation. The CBN has announced a Resident Examiners' Program will commence from January 2009, with CBN posting staff to each of the banks who will monitor and supervise the activities of the banks daily and report back to CBN headquarters. Industry observers have expressed their concern that resident examiners could be compromised. Certainly there is dirt hiding under the carpet. One businessman told Econcouns recently that government agencies were depositing very significant program funds with commercial banks under the excuse that rule of law and due process required a deliberate (slow) pace of releasing such funds to their intended uses. The businessman said that banks were able to treat these as zero interest deposits, but in reality the official ordering the deposit would receive 14 percent personally for providing the funds to the commercial bank and banks would then relend the funds at 20 percent. An important guide to nipping the bank failures in the bud before they become systemic is to increase the disclosure requirements needed in financial reports. A separate decision in the August 5 CBN communique that announced the cancellation of the common accounting year required banks to fully disclose to the public their deposit and base lending rates. The issue on the table now is enforcement. Zero tolerance for false reporting and infringement is essential, while the CBN needs to overhaul it's supervisory capacity. Nigeria does need to try to avoid a round of bank failures, but in the long run it is more important that it strengthen bank supervision. That won't be easy, both in terms of will and capacity. Industry contacts have expressed to both Embassy and ConGen their concern that neither the CBN nor Nigeria-based accounting firms have the capacity to rigorously examine the commercial banks' books. End comment.

PIASCIK